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SUBJECT: BRAZILIAN BUSINESS PERSPECTIVES ON OPEN SKIES

REF: 09 BRASILIA 1319; 09 SAO PAULO 630

11. (SBU) Summary: In recent meetings with Brazilian flag carrier TAM, low cost carrier Azul, U.S. airlines, Brazilian tour operator Agaxtour, FEDEX and the GOB-owned airport concessionaire (Infraero), representatives acknowledged the benefits of a potential Open Skies Agreement (OSA) between the United States and Brazil as bilateral economic ties grow and Brazil's expanding middle class (ref B) travels more. They also cited many challenges to an agreement including the competitive disadvantages of Brazilian carriers, infrastructure limitations and a foreseeable shortage of trained personnel to implement increased security and safety requirements. ANAC's President Solange Vieira has also expressed doubts regarding the feasibility of beginning OSA negotiations in 2010. Nonetheless, with domestic demand for air services growing 42 percent over the last year and low-cost carriers Azul, Webjet and Oceanair gaining market share, business interest in an OSA appears to be growing. Discussions with industry contacts suggest that fostering nascent direct partnerships between Brazilian and U.S. airports, exploring a cargo OSA, or working toward expanding cargo and passenger frequencies could create a foundation for moving forward on a comprehensive OSA. End Summary

Growing Demand Spurs Interest as Fears Linger

12. (SBU) With Brazil's economy and middle class growing steadily and major international events looming, (e.g. World Cup in 2014, Olympics in 2016) demand for passenger and cargo services are climbing. According to the Brazilian National Civil Aviation Agency (ANAC), the number of domestic passengers has tripled within the last decade to over 60 million per year. Consulate General Sao Paulo became the busiest non-immigrant visa issuing post in the world in FY-09. Brazilian airlines, tour agency, and Infraero representatives we spoke with acknowledged that an Open Skies Agreement would be a natural framework for promoting fair competition. Nonetheless, contacts such as Infraero Director of Operations at Guarulhos Airport, Percio Rosa da Silva, acknowledge that insufficient infrastructure, restrictive labor laws and onerous taxes, place local industry at a competitive disadvantage to U.S. carriers. As such, Silva and others suggest that a lengthy phase-in period or other staged implementation would be necessary

to reduce asymmetries. Jose Mauricio Mollo, the president of the National Airline Union (SNEA), said that many Brazilian airlines actually favor an Open Skies Agreement between South American nations prior to one with North American or European airlines, as a means of reducing the competitive disadvantages of Brazilian carriers.

Clear Benefits

¶3. (SBU) While concerned about competitiveness challenges local industry would face under an OSA with the United States, most private sector contacts including Paulo Castello Branco of TAM and Luiz Camillo of United Airlines also acknowledge the benefits of increased trade and travel for lowering consumer costs, enhancing productivity and spurring economic growth. Adalberto Febeliano of Azul says that an OSA could also bolster tourism, already growing annually at 5 percent. Brazilian contacts also expect decentralization of the market to lead to partnerships and eventually joint ventures, similar to those that exist between U.S. and European carriers. While the American carriers are more vocal proponents than the Brazilian carriers, all parties agree that forming partnerships brings opportunity for competition. Brazilian low cost airlines, in particular, are eager to partner with American carriers on code-sharing to extend their internal routes

to U.S. destinations. Conversely, U.S. carrier representatives such as Luiz Camillo of UAL view an OSA as key to competing for slots in the tight Sao Paulo and Rio de Janeiro markets. U.S. companies cite their recent entries into Northeast Brazil, a traditionally less competitive and profitable area, as evidence of the growth potential unleashed with liberalized air frequencies. Agaxtour owner, Aldo Leone, echoed the call for an OSA, saying the competition and partnerships spurred by an OSA translate into lower prices and more choices for the growing number of Brazilians with disposable income for domestic and international travel.

But Challenges Remain

¶4. (SBU) Despite the clear benefits of an OSA, business contacts foresee various impediments to liberalizing passenger and cargo services in the near future. Brazilian airport infrastructure and congestion pose a particular challenge. For example, a recent realignment of 381 slots in Congonhas Airport designed to spur competition may actually drive some of the low cost players out of the airport. Guarulhos international airport is approaching its limit even at non-peak times. A third Guarulhos terminal is planned, but groundbreaking has not started even as the 2014 World Cup and 2016 Rio Olympics approach. In the meantime, Azul, Gol and other low-cost carriers have expanded their presence at nearby Viracopos airport in Campinas. As a result, Viracopos will receive an additional 6.5 million passengers per year beginning in 2010, according to Azul President Pedro Janot. Though there are plans for another airport in the GOB's national public infrastructure investment program (PAC), Infraero Guarulhos Operations Director Rosa da Silva said it is unlikely there will be any development within the next four years. Under this extreme congestion, U.S. carriers face significant challenges in expanding their routes to the lucrative Sao Paulo market, even in partnership with the Brazilian airlines.

¶5. (SBU) Infraero views potential partnering with U.S. carriers as an opportunity to refine the Brazilian security requirements in accordance with the stringent U.S. levels. Percio Rosa da Silva emphasized that Brazil would be the ideal partner in Latin America for an OSA, given the size and commonalities of both nations. He added that Brazil is the regional leader, providing a model and

training for other Latin American nations. However, he said that many more personnel trained in U.S. standards would be needed to accommodate the increase in flights to/from the U.S. anticipated under an OSA. Da Silva cited more training as a key requirement, stressing the lack of a private sector institution in Brazil that prepares flight controllers and administrators of airports. He noted that Embry Riddle University of Daytona, Florida is in the process of establishing an agreement to offer aeronautical training courses in Brazil and suggested such educational cooperation would be necessary to prepare for an OSA.

¶6. (SBU) In a recent Washington meeting between ANAC's President Solange Vieira and DOS Aviation Negotiations Director Kris Urs, Vieira expressed doubts about initiating OSA discussions with the U.S. in 2010 given competing priorities at ANAC. Vieira explained that ANAC was committed to concluding OSA negotiations with South American partners and an Air Transportation Agreement (ATA) with the European Union before beginning negotiations with the U.S. Citing a passenger or cargo based OSA with the U.S. as a hard sell within the GOB, Vieira suggested that the U.S. instead request additional frequencies as needed under the current U.S./Brazil ATA. When pressed about the difficulties in requesting additional frequencies to Sao Paulo's Guarulhos airport, Brazil's largest and most preferred international gateway, due to its operational

constraints, Vieira confirmed that the 45 flight per hour limit imposed in 2009 by ANAC, would be managed under International Air Transport Association (IATA) world scheduling guidelines, offering a more reliable scenario for increasing there. (Note: DOT is going to confirm this with IATA. End Note)

Moving forward...

¶7. (SBU) Business representatives tell us that moving an OSA forward will require more dialogue among the airlines, consumers and government. The airlines and tour companies, represented by Agaxtour and Infraero, all point to Brazilian bureaucracy and competition fears as major stumbling blocks towards implementing an OSA. Nevertheless they say direct airport agreements, such as the cooperative exchange program between Guarulhos and Miami international airports have enhanced relationship building and reduced Brazilian carriers' fears of competition. Such an agreement aims to officially link both airports, committing each to exchange information pertaining to passenger and cargo industries as well as create working groups to promote additional areas of cooperation. Infraero is already seeing the benefits from information and security exchange, formulating a preliminary study about broader airport cooperation. Shipping industry representatives suggest another potential starting point for an OSA could be cargo, as 50 percent of the cargo shipped from Brazil's main cargo airport (Guarulhos) is destined for the United States. Increased cargo options and simplified requirements under an OSA would expedite delivery and reduce shipping costs - a major expense for Brazilian manufacturers and importers.

¶8. (SBU) Cargo contacts, including FEDEX, are strong proponents of an OSA. Jim Davis, of FEDEX's Sao Paulo office, stated that an OSA would provide his cargo shippers flexibilities to expand their networks. FEDEX currently has five frequencies per week between Viracopos airport (in Campinas, an hour from Sao Paulo) and their Memphis hub, in addition to intra-South American flights. Bruno Ramon Ariki of Brazilian freight forwarder Expeditors International, similarly told Econoff that enhanced code-sharing would decrease freight rates while offering more variety for Brazilian freight forwarders to use other airline routings. Ariki said that Brazil's current restrictions on cargo routes major lanes represent a major cost hurdle for shippers. In addition to airline code sharing, Ariki envisions that Brazilian freight forwarders may

benefit from the possibility of sales offices in the USA, which could convert earnings and remittances to Brazil without restrictions.

COMMENT

¶9. (SBU) The Brazilian civil aviation market has opened slowly in recent years and an OSA would further decentralize the current duopoly in passenger service (TAM and Gol posses 85% of market share), which would benefit the Brazilian consumer. While competitiveness concerns by Brazilian carriers and capacity issues, derived mostly from infrastructural limitations, represent a challenge to reaching an OSA, growing demand for air services in Brazil and increased concerns about the global competitiveness of Brazilian manufacturers (e.g. shipping costs) provide a potential foothold for U.S. airlines to enter the growing Brazilian market. Above all, there is a need for increased dialogue among the stakeholders, with the backing of the GOB (Reftel A), to advance an OSA. Although 2009 saw a significant increase in civil aviation security and safety cooperation between the USG and GOB, OSA

negotiations in the near-term appear unlikely. In the meantime, as American carriers strive to increase their presence and profits, building on nascent airport-to-airport partnerships and leveraging increased demand for passenger and cargo services into additional frequencies may be a means of moving forward. End Comment.

¶10. (U) This cable was coordinated/cleared by Embassy Brasilia.
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